

IT 95-88

Tax Type: INCOME TAX

Issue: Federal Change (Individual)
Reasonable Cause on Application of Penalties Assessed

STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
SPRINGFIELD, ILLINOIS

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THE DEPARTMENT OF REVENUE      )      Docket #
OF THE STATE OF ILLINOIS      )      SS #
                               )      Track #
                               )
                               )      Barbara S. Rowe
XXXXXX                        )      Administrative Law Judge
                               )
Taxpayer                      )
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RECOMMENDATION FOR DISPOSITION

SYNOPSIS This matter is properly before the Office of Administrative Hearings of the Illinois Department of Revenue (the "Department"), pursuant to a timely protest filed on behalf of XXXXX (the "Taxpayer") to the notice of deficiency issued February 23, 1995 for the taxable years ending December 31, 1990 and 1991. The notice was in the amount of \$5,761.00 and was based upon a completed and settled Federal change. The notice imposed an increase in tax liabilities and penalties under 35 ILCS 5/1005 for failure to pay the entire tax liability by the due date of the return. In their protest, the taxpayer stated that they were willing to pay the tax and interest in order to close the case but they were protesting the penalties for late filing since they promptly filed the 90 and 91 income tax returns.

The taxpayer did not request a hearing, accordingly this matter is being decided based upon the documents contained in the Department file including all documentation submitted by the taxpayer. The issue to be decided is whether the taxpayer is liable for a penalty pursuant to 35 ILCS 5/1005. It is recommended that the Director uphold the penalty.

FINDINGS OF FACT

1. The Department issued a notice of deficiency on February 23, 1995 pursuant to Section 904(c) of the Illinois Income Tax Act in the amount of \$5,761.00 for the taxable years ending December 31, 1990 and 1991. The basis of the notice was a completed and settled federal change as referenced by Sections 506(a) and (b) (35 ILCS 5/506(a) and (b)) of the Illinois Income Tax Act. (Dept. Ex. No. 1)

2. The notice included a penalty under Section 1005 of the Illinois Income Tax Act because the taxpayer did not pay the entire tax liability by the due date. (Dept. Ex. No. 1)

3. On March 17, 1995, the Department received an administration and procedure protest filing form from the taxpayer stating that a hearing was not requested but that the penalty was not acceptable because they did not anticipate the assessment and they paid the entire bill on the proper due date. (Dept. Ex. No. 2)

4. On June 15, 1995 the Department sent the taxpayer a notice of inadequate protest requesting the grounds on which the protest was based. (Dept. Ex. No. 3)

5. On June 26, 1995, the taxpayer's representative responded to the notice of inadequate protest stating again that the taxpayer did not request a hearing but that the penalties for late filing were being protested because the taxpayer promptly filed the 1990 and 1991 income tax returns and paid the taxes. (Dept. Ex. No. 4)

6. The Federal audit for this taxpayer was conducted by examiner XXXXX in Chicago district 36. The Federal changes were finalized on September 23, 1993. At the bottom of the taxpayer's Federal reporting form 45490A-CG is the following language:

The Internal Revenue Service has agreements with State tax agencies under which information about Federal tax, including increases or decreases, is exchanged with the States. If this change affects the amount of your State income tax, you should file the State form. (Dept. Ex. No. 5)

7. The Department sent the taxpayer a letter on March 18, 1994 stating that the Department has been notified of an adjustment to the taxpayer's Federal return. In the letter the Department requested that the taxpayer file the enclosed IL-1040-X and remit the additional tax and interest due. (Dept. Ex. No. 6)

CONCLUSIONS OF LAW Article IX, 3 of the Illinois Constitution of 1970, enables the legislature to enact an Income tax. It provides in part as follows:

- (a) A tax on or measured by income shall be at a non-graduated rate. At any one time there may be no more than one such tax imposed by the State for State purposes on individuals and one such tax so imposed on corporations. In any such tax imposed upon corporations the rate shall not exceed the rate imposed on individuals by more than a ratio of 8 to 5.
- (b) Laws imposing taxes on or measured by income may adopt by reference provisions of the laws and regulations of the United States, as they then exist or thereafter may be changed, for the purpose of arriving at the amount of income upon which the tax is imposed.

Section 506 of the Illinois Income Tax Act (35 ILCS 5/506) deals with Federal income tax returns and the taxpayer's responsibilities to the State of Illinois in conjunction with those returns. In particular, 506(b) states:

- (b) Changes affecting federal income tax. In the event the taxable income, any item of income or deduction, or the income tax liability reported in a federal income tax return of any person for any year is altered by amendment of such return or as a result of any other recomputation or redetermination of federal taxable income or loss, and such alteration reflects a change or settlement with respect to any item or items, affecting the computation of such person's base income for any year under this Act, or in the number of personal exemptions allowable to such person under Section 151 of the Internal Revenue Code, such person shall notify the Department of such alteration. Such notification shall be in the form of an amended return or such other form as the Department may by regulations prescribe, shall contain the person's name and address and such other information as the Department may by regulations prescribe, shall be signed by such person or his duly authorized representative, and shall be filed not later than 120 days... after such alteration has been agreed to or finally determined for federal income tax purposes or any federal

income tax deficiency or refund, tentative carryback adjustment, abatement or credit resulting therefrom has been assessed or paid, whichever shall first occur.

The taxpayer did not file an amended return within 120 days after the finalized Federal change. The taxpayer did not respond to the letter dated March 18, 1994, wherein the Department requested that they file an amended return and pay the tax and interest due. It is Departmental policy to issue a notice of deficiency only after 120 days have elapsed following the finalization of a Federal change. In this case, the notice of deficiency was issued 518 days after the finalized Federal change.

Section 1005 of the Illinois Income Tax Act, (35 ILCS 5/1005(a)) imposes a penalty for underpayment of the tax. Subsection (a) of the Act states:

In general. If any amount of tax required to be shown on a return prescribed by this Act is not paid on or before the date required for filing such return (determined without regard to any extension of time to file), a penalty shall be imposed in the manner and at the rate prescribed by the Uniform Penalty and Interest Act.

The taxpayer asserts that they paid the tax on the due date and therefore should have the penalties waived. At issue is not whether they paid the initial tax on the due date, but rather whether they paid the tax that was due in a timely manner once the Federal change was finalized. This was not done and the taxpayer has not shown a reasonable cause why the penalties should be waived.

I therefore recommend that the Director uphold the notice of deficiency in its entirety, including the 1005 penalty.

Respectfully Submitted,

Barbara S. Rowe
Administrative Law Judge

September 22, 1995